DIRECT TESTIMONY

OF

JOHN W. FLITTER

ON BEHALF OF

SOUTH CAROLINA ELECTRIC & GAS COMPANY

DOCKET NO. 2002-2-E

Q. STATE YOUR NAME AND BUSINESS ADDRESS.

A. John W. Flitter, 111 Research Drive, Columbia, South Carolina.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

I am General Manager of the Fossil Hydro Procurement Department of South Carolina Electric & Gas Company (SCE&G).

Q. DESCRIBE YOUR EDUCATIONAL BACKGROUND AND YOUR BUSINESS EXPERIENCE.

A. I graduated from the University of South Carolina in 1966 with a Bachelor of Science Degree in Business Administration; majoring in Accounting. I was employed by South Carolina Electric & Gas Company in September, 1966 in the Budget and Statistic Department. I have held supervisory and management positions with the Company, beginning in 1973, which include Supervisor-Accounting Special Studies, Manager-Cost Studies and Load Research, Manager-Rate Regulation, Manager-Fossil Fuel Supply and my current position of General Manager-Fossil Hydro Procurement. I have previously presented testimony on numerous occasions before this Commission and the Federal Energy Regulatory Commission for both South Carolina Electric & Gas Company and South Carolina Generating Company (GENCO).

Q. SUMMARIZE YOUR DUTIES AS GENERAL MANAGER OF FOSSIL HYDRO PROCUREMENT AS THEY RELATE TO FOSSIL FUEL.

A. I am responsible for the planning, development, analysis and implementation of system-wide strategies for the purchase and delivery of fossil fuels for electric generation in a manner consistent with the Company's objective to obtain the greatest ultimate value for each dollar spent, consistent with maximum reliability. I also perform these functions for South Carolina Generating Company's Williams Station.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?

A. The purpose of my testimony is to describe procurement and delivery activities for fossil fuel used in electric generation for SCE&G and GENCO.

Q. WHAT ARE THE OBJECTIVES OF THE COMPANY'S FUEL PURCHASING PRACTICES?

A. The objectives of the Company's fossil fuel purchasing practices are to provide a reliable supply of fossil fuels, of required quality, at reasonable prices.

Q. HOW DOES THE COMPANY ASSURE THE SUPPLY OF COAL NECESSARY TO ENABLE THE COMPANY TO PROVIDE RELIABLE SERVICE?

A. The strategy to meet this objective is developed based upon our projected burn levels, our anticipated coal inventory levels and the anticipated availability and price of coal in the marketplace. Of course, maximum assurance of supply could be achieved hypothetically by securing long term contracts for our total requirements. However, doing so would prevent the Company from taking advantage of potentially favorable supply and price changes in the short-term and spot markets. As an effective supplement to our long-term agreements, our short-term contracts have enabled us to combine assurance of supply with an ability to meet changing market conditions over one or two-year periods. In addition, we have maintained an active role in the spot market, making purchases from reliable suppliers to meet requirements not satisfied by our contracts. Furthermore, our long-term contracts contain variable quantity provisions which enable the Company to increase or decrease contract quantities under

certain conditions. These provisions assure us that additional coal will be available under those contracts should it be in our best interest to expand our purchases under them. They also allow us to decrease purchases should our participation in the short-term or spot markets be more advantageous. Finally, we strive to maintain, on average, a coal inventory equal to approximately two (2) months of anticipated consumption. This inventory serves several functions. It serves to moderate the overall cost to our ratepayers, while, at the same time, protecting us against problems in availability, production and deliverability of coal. In some instances, we rely upon inventory to meet supply requirements because of unfavorable market conditions, although such reliance must be exercised with careful consideration of future requirements and operating conditions.

Q. HOW DOES THE COMPANY ACHIEVE THE OBJECTIVE OF AN ASSURED QUALITY OF THE COAL IT NEEDS?

A. The Company's contracts for coal supplies and our orders for spot market purchases of coal identify the quality specifications of the coal which we require. Quality characteristics include: BTU content, moisture content, ash content, ash fusion temperature, volatile matter, fixed carbon, sulfur content, grindability and size. Our contracts for coal supplies and our purchase orders for spot market purchases include upward cost adjustment provisions for shipments which exceed the guaranteed BTU specification and downward cost adjustment provisions for failure of the shipments to meet the guaranteed BTU content. Also, most of our long and short term contracts provide for reduced sulfur content as part of our strategy for compliance with Phase II of the Clean Air Act. With respect to quality characteristics, our contracts provide for cancellation or rejection, at our option, for failure of the supplier to meet any of the specifications identified in the contract. With respect to spot market deliveries, the

failure of the supplier to meet any of the required specifications can result in the cancellation or rejection of deliveries under the purchase order.

Q. HOW DOES THE COMPANY EVALUATE THAT PART OF THE COMPANY'S PURCHASING OBJECTIVE RELATED TO "REASONABLE PRICE"?

A. In our analysis of fuel purchasing, the reasonableness of the price which we pay for coal cannot be realistically separated from the assurance of an adequate supply of coal meeting our quality specifications. Price is a concept contingent on supply, quality and location and is ultimately related to the value of the coal in the operation of our generating plants, expressed on the basis of cost per MBTU. Price incorporates the cost of fuel, pricing mechanisms and transportation, and must be evaluated under market conditions which are current at the time of the establishment of the price. For example, under certain market conditions, the establishment of a firm price per ton for coal may be preferable to a price which is adjusted periodically based on independent indexes. Under other conditions, the periodic adjustment mechanism may be preferable. Furthermore, it can be considered advantageous to have a variety of pricing mechanisms among coal contracts in order to mitigate or avoid the effects on prices produced by changes in market conditions or indexes which would be exaggerated if pricing mechanisms were identical in all coal contracts.

Another consideration in pricing is the information concerning various market conditions which can be useful in evaluating the reasonableness of price. We continually review published data from a variety of public and governmental sources, and are in continuous contact with market participants who provide information concerning various market conditions which we evaluate carefully for our purchasing decisions. Such market data are used in our analysis of current or prospective coal costs to determine whether those costs are generally comparable to the market. Because

prices are contingent upon current, and to some extent, projected, market conditions and factors unique to each buyer, a simple comparison of coal costs experienced by several purchasers, even electric utilities in the same geographic region, would not itself establish the reasonableness of the prices paid for coal supplies. In the final analysis, there is no single gauge or standard against which to measure the reasonableness of a particular price. Rather, price must reflect the value of the fuel, the supply requirements and transportation considerations of the buyer, and the corresponding economic and supply conditions in the marketplace at the time a contract is made. In light of those considerations, the Company has been able to achieve its coal purchasing objective at a reasonable cost to the Company and its customers.

Q. SUMMARIZE THE QUANTITY, QUALITY, AND TERM OF THE COMPANY'S COAL CONTRACTS.

A. During the period March, 2001 through February, 2002, the Company purchased approximately 6.0 million tons of coal under long term and short term contracts which represented approximately 89.9% of the requirement for the Company's five coal-fired stations, GENCO's Williams Station and Savannah River Site. For the March, 2002 through February, 2003 period, the Company projects to have under long term contract with 8 suppliers 5.1 million tons of coal with minimum contract tonnage representing approximately 85.1% of the total receipts. The quality ranges are from 12,000 to 12,800 BTU with a sulfur content of from 0.75% to 1.5%. These contracts are for a period of three (3) years with options to renew or extend for as long as six (6) additional years. The amount of coal under contract will vary from year to year. In some of our coal contracts, we have been successful in negotiating fixed pricing whereby the price is not changed for a fixed period of time, usually for the full term of the contract. In other coal contracts price adjustments are negotiated for predetermined adjustment amounts.

Q. WHAT PRICES HAS THE COMPANY PAID TO COAL PRODUCERS FROM

MARCH 2001 THROUGH FEBRUARY 2002?

A. Exhibit No. _____ (JWF-1) entitled, "Coal Purchased For Steam Plants", shows the average cost per MBTU of coal purchased in March, 2001 through February, 2002. Based on the long term and short term contracts and the purchases of spot coal during that period, we have seen the producer cost of coal vary in price from a weighted average high of $1.1989 per MBTU ($30.35 per ton) in December, 2001 to a weighted average low of $1.0074 per MBTU ($25.44 per ton) in March 2001.

Q. WHAT HAS BEEN THE RECENT PRICING TREND FOR THE COAL INDUSTRY?

A. As early as the fall of 2000, the price of coal had begun to escalate and continued to escalate through the spring of 2001. Since then, prices for both short tem spot and long term contract coal have declined. However, the decline in short term spot coal prices have been significant as compared to long term contract prices.

Q. WHAT ARE THE MAJOR FACTORS THAT HAVE INFLUENCED COAL MARKET CONDITIONS?

A. Several key factors which have impacted market conditions are as follows: (1) Strict new environmental laws have delayed new mine permits; (2) three major coal producers have filed Chapter 11 while one more has been dissolved in Chapter 11; (3) several major producers have had production problems and marginally profitable mines have been shut down; (4) abnormally mild weather in 2001 and early 2002; and (5) a down turn in the economy due to the 9/11 tragedy.

Q. HOW HAS THE GENERAL AVAILABILITY OF COAL BEEN AFFECTED?

A. The availability of coal, beginning in the late fall of 2000, began to decline. As of March, 2001, spot coal availability for second quarter 2001 deliveries was essentially non-existent. Production began to catch up with demand in early fall of 2001. Recently we have experienced a short term oversupply of coal in the short term spot market

created by extremely mild weather during 2001 and early 2002 as well as the down turn in the economy.

Q. HOW HAVE FREIGHT COSTS VARIED FROM MARCH 2001 THROUGH FEBRUARY 2002?

A. My Exhibit No. _____ (JWF-1) shows the average freight costs per MBTU for coal purchased for each month. During that period, the freight costs varied from a weighted average high of $0.5038 per MBTU ($12.75 per ton) in October, 2001 to a weighted average low of $0.4546 per MBTU ($11.50 per ton) in February, 2002.

Q. HOW HAVE DELIVERED COSTS FOR COAL TO INCLUDE FREIGHT VARIED FROM MARCH 2001 THROUGH FEBRUARY 2002?

A. Exhibit No. _____ (JWF-1) shows the average delivered cost per MBTU of coal purchased in March, 2001 through February, 2002. During that period, we have seen the delivered cost of coal vary in price from a weighted average high of $1.6644 per MBTU ($42.12 per ton) in October, 2001 to a weighted average low of $1.4919 per MBTU ($37.67 per ton) in the month of March, 2001.

Q. WHAT FREIGHT RATE CHANGES HAS THE COMPANY EXPERIENCED?

A. There have been no freight rate changes during this review period.

Q. HOW DOES THE COMPANY CONTROL FREIGHT CHARGES?

A. We are continually communicating with our freight carriers regarding innovative ways by which we can moderate not only present but also future freight costs for the movement of coal to our Company. The Company is addressing various issues with CSX Transportation, Inc. (CSX) and the Norfolk Southern Corporation (NS) to include increased freight rate discounts, minimized future freight rate adjustments, and increased incentives for additional tonnages moved.

Q. WHAT HAS BEEN THE RECENT PRICING TREND IN THE NO. 2 FUEL OIL INDUSTRY?

A. During the past year, delivered prices have varied from a weekly low of $0.5102/gallon in December, 2001, to a weekly high of $.8785/gallon in June, 2001. Exhibit No. _____ _____ (JWF-2) shows the average delivered #2 fuel oil prices for Hagood Gas Turbine in March, 2001 through February, 2002.

Q. ARE THERE ANY OTHER THINGS THE COMPANY HAS DONE TO MITIGATE FUEL RELATED EXPENSES THAT WILL IMPACT FUEL COSTS?

A. Effective January 1, 2000, Phase II of the Clean Air Act of 1990 called for electric utilities to reduce sulfur dioxide (SO2) emissions. A SO2 Emission Allowance Trading Market was established by the Environmental Protection Agency (EPA) to assist utilities in managing the costs of complying with these new regulations. The Company has purchased SO2 allowances as part of our overall strategy to compensate for our SO2 emissions.

Q. HAS SCE&G MADE EVERY REASONABLE EFFORT TO MINIMIZE ITS FUEL PROCUREMENT COSTS?

A. Yes. As outlined above, we have made every reasonable effort to obtain reliable, high quality supplies of fuel and transportation at the lowest possible cost to our customers.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.

South Carolina Electric & Gas

COAL PURCHASED FOR STEAM PLANTS
MARCH 2001 THROUGH FEBRUARY 2002

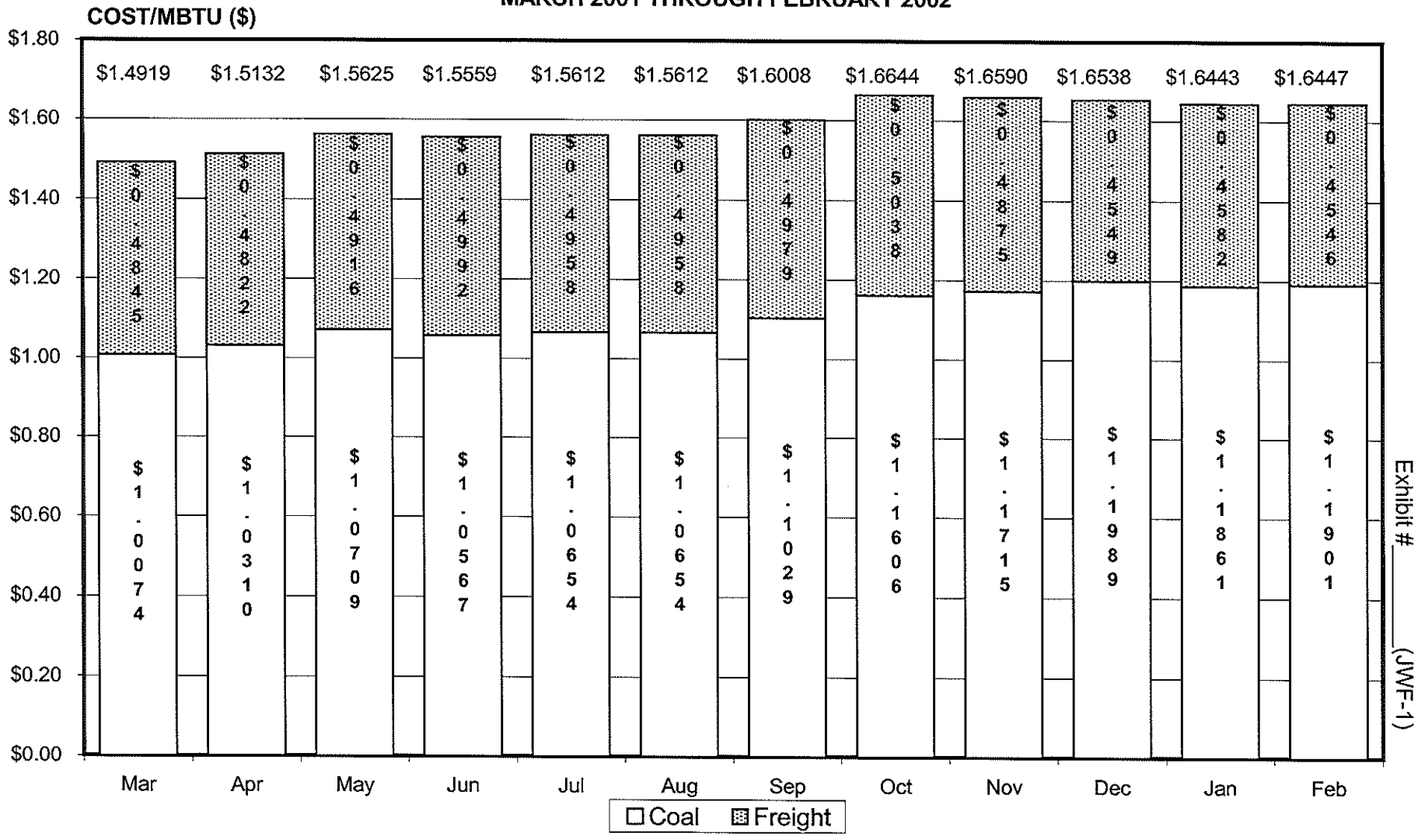

Exhibit #_____(JWF-1)

Delivered #2 Fuel Oil Prices
Hagood Gas Turbine
Charleston, SC

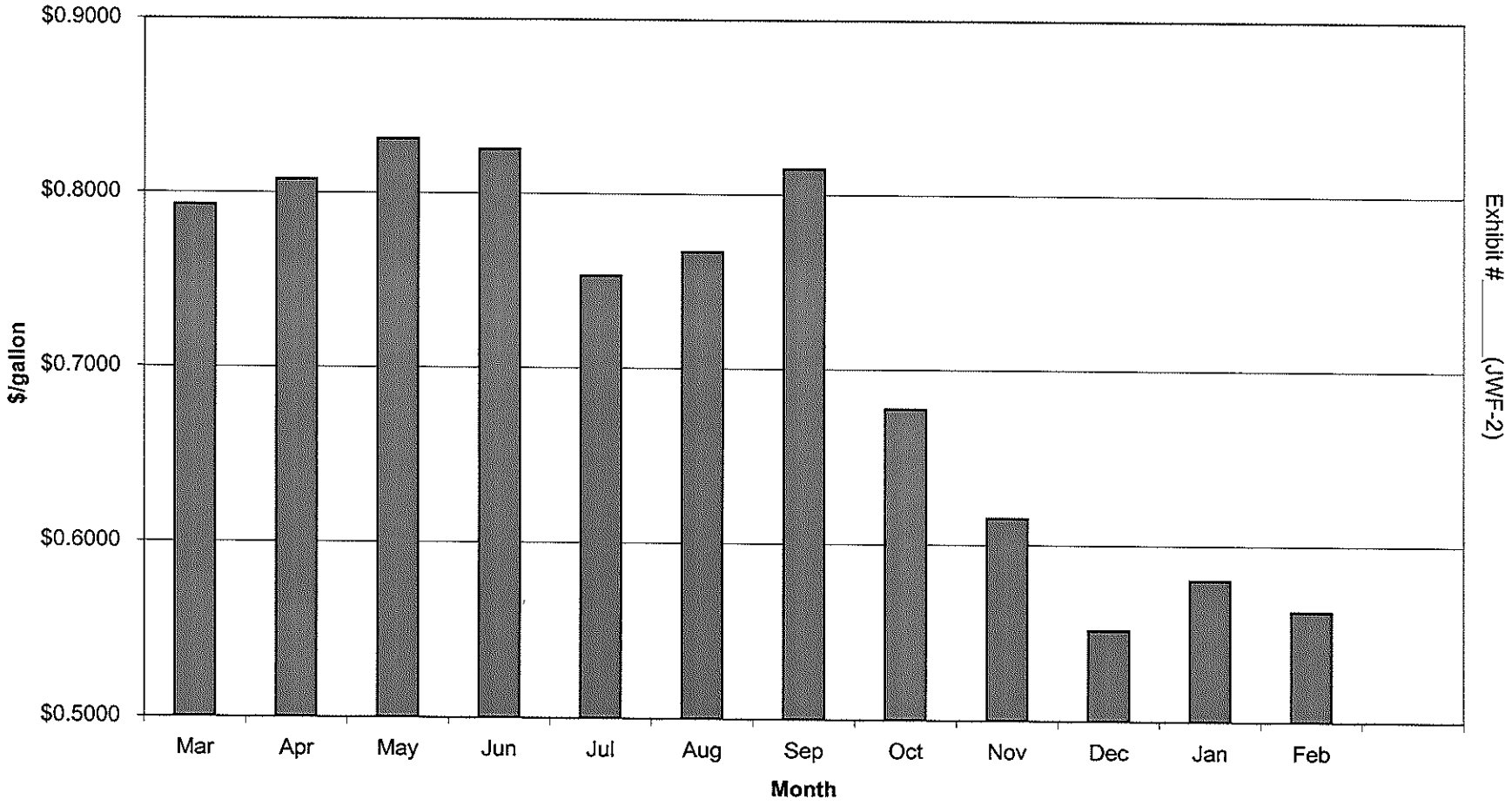

Exhibit #____(JWF-2)